(7)

No. 90-693

In the
Supreme Court of the United States

OCTOBER TERM, 1990

CURTIS REED JOHNSON,
PETITIONER,

v.

HOME STATE BANK,
RESPONDENT.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT
OF APPEALS FOR THE TENTH CIRCUIT

Brief of Consumers Education and Protective Association, Inc. and Jeanne Browning as Amici Curiae in Support of Petitioner

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INTEREST OF AMICI CURIAE

Amicus Consumer Education and Protective Association, Inc. (CEPA) is an organization of consumers which is dedicated to advancing the cause of consumer rights and which works in support of statutory remedies designed to alleviate the burdens faced by low and middle income consumers. CEPA considers the remedies afforded debtors under the Bankruptcy Code to be an important means of ameliorating the human costs which arise in an economic system in which business failure, with concomitant layoffs and unemployment, regularly occur. Many individuals, who suffer an interruption of reduction of their income due to circumstances beyond their control, must necessarily resort to the remedies provided by chapters 7 and 13 of the Bankruptcy Code in order to address

the burden of their debt or to reorganize their financial affairs. For many persons, chapter 13 is the only means available for setting up affordable payment plans so that they can satisfy their debts and retain the modest amount of property they have acquired -- especially their most important assets, their homes.

Amici Jeanne Browning is an individual who owns residential property encumbered by a mortgage. Browning is currently in a chapter 7 bankruptcy case, necessitated by unemployment. The mortgage on her home is in default. Should she find employment and obtain sufficient income after her chapter 7 case is completed to make it feasible to save her home through chapter 13 relief, she may wish to avail herself of that remedy.

SUMMARY OF ARGUMENT

The decision of the court below prevents a debtor who has been discharged of _in personam_ liability on a mortgage debt from listing the remaining _in rem_ liability as a debt in a chapter 13 bankruptcy. This decision is at variance with the plain language of the Bankruptcy Code and its legislative history. Further, the decision invents a _per se_ rule of eligibility for chapter 13 relief that has no basis in the Code and is inconsistent with the purpose and policies of chapter 13. If the lower court's decision is affirmed, the availability of bankruptcy relief for consumer debtors would be severely impaired.

ARGUMENT

I. BOTH THE PLAIN LANGUAGE OF THE BANKRUPTCY CODE AND ITS LEGISLATIVE HISTORY ESTABLISH CONGRESS' INTENT TO DEFINE THE TERM "CLAIM" TO INCLUDE IN REM OBLIGATIONS

A. This Court's Inquiry Need Go No Further Than An Examination Of The Text Of Sections 101(4) And 102(2) Of The Bankruptcy Code

The issue in this case is whether the term "claim," as defined in the Bankruptcy Code, 11 U.S.C. §101(4),[1] encompasses a mortgage lien which encumbers a debtor's property and remains due after the debtor's

[1] Until November 1990, the Bankruptcy Code's definition of the term "claim" was codified at 11 U.S.C. §101(4). In the Crime Control Act of 1990, Pub L. No. 101-647, Congress amended section 101 of the Bankruptcy Code, 11 U.S.C. §101, to add a new subparagraph (3) and to redesignate former subparagraphs (3) through (31) as subparagraphs (4) through (32). The amendment is effective November 29, 1990 with respect to all cases filed on or after that date. Thus, for cases filed after November 29, 1990, the definition of the term "claim" is now codified at 11 U.S.C. §101(5). To avoid confusion, and because the amendment does not apply to this case, this brief will cite to the former codification of the definition, 11 U.S.C. §101(4).

in personam liability on the secured debt has been discharged in a prior bankruptcy. If such an obligation is a "claim," then a debtor may provide for payment of the obligation under the terms of a chapter 13 plan. See 11 U.S.C. §1322(b).

As in all cases of statutory construction, the starting point in this case must be the statutory language itself. Pennsylvania Department of Public Welfare v. Davenport, 110 S.Ct. 2126, 2130 (1990); United States v. Ron Pair Enters., Inc., 109 S.Ct. 1026, 1030 (1989). "[T]he strong presumption [is] that Congress expresses its intent through the language it chooses." Immigration and Naturalization Servs. v. Cardoza-Fonseca, 480 U.S. 421, 432 n.12 (1987). Where the terms of the statute are unambiguous, only the "most extraordinary showing of contrary

intentions" from the legislative history would justify limiting the statute's plain language." Garcia v. United States, 469 U.S. 70, 75 (1984). As long as the framework of the Code is coherent and consistent, there is generally no need to look beyond the plain language. Ron Pair, 109 S.Ct. at 1030.

In this case, the language of the Code is clear, making resort to legislative history unnecessary. In the text of the statute, Congress has unambiguously expressed its intent to include in rem obligations within the scope of the definition of the term "claim."

B. Sections 101(4) and 102(2), Read Together, Unambiguously Express Congress' Intent To Include In Rem Obligations Within The Definition Of The Term "Claim"

1. 11 U.S.C. §101(4)

Section 101(4) of the Bankruptcy Code

defines the term "claim" as a:

> (A) right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured; or
>
> (B) right to a equitable remedy for breach of performance if such breach gives rise to a right to payment, whether or not such right to an equitable remedy is reduced to judgment, fixed, contingent, matured, unmatured, disputed, undisputed, secured, or unsecured;

11 U.S.C. §101(4).

Under §101(4), the initial inquiry must be whether an in rem obligation gives rise to a "right to payment." Recently, this Court observed that, in enacting this definition, "Congress chose expansive language" and that to the extent the phrase "right to payment" is modified in §101(4), the modifying language "reflects Congress' broad rather than restrictive view of the class of obligations that qualify as a

'claim.'" Davenport, 110 S.Ct. at 2130. See also Ohio v. Kovacs, 469 U.S. 274, 279 (1985) (claim broadly construed to include obligation to clean up a hazardous waste disposal site).[2]

When does an obligation give rise to a right to payment? Last term in Davenport, this Court considered whether a criminal court sentence obliging an individual to make monetary restitution is a right to payment and therefore, a claim under the Bankruptcy Code. The Court held that a criminal restitution obligation is a bankruptcy claim. The Court rejected the

[2] Courts have consistently interpreted the scope of the term "claim" broadly. See, e.g., In re Remington Rand Corp., 836 F.2d 825, 829 (3d Cir. 1988) ("all possible legal obligations"); In re Robinson, 776 F.2d 30, 36 (2d Cir. 1985) ("broadest possible"), rev'd on other grounds, 479 U.S. 36 (1986); In re Baldwin-United Corp., 48 B.R. 901, 903 (Bankr. S.D. Ohio 1985) ("all encompassing"); In re Smith Jones, Inc., 26 B.R. 289, 293 (Bankr. D. Minn. 1982) ("sufficiently broad to cover any possible obligation").

argument that the definition of the term claim should be construed with reference to either the purposes of restitution or the methods of enforcement. Rather, the Court relied solely on the commonly understood meaning of the statutory phrase, concluding that "[t]he plain meaning of a 'right to payment' is nothing more than an enforceable obligation." 110 S.Ct. 2131.[3]

The reasoning employed by the Court in Davenport controls the outcome of this case. It is difficult to conceptualize how respondent's mortgage against petitioner's real property is anything other than an "enforceable obligation." If petitioner

[3] "A fundamental canon of statutory construction is that, unless otherwise defined, words will be interpreted as taking their ordinary, contemporary, common meaning." Perrin v. United States, 444 U.S. 37, 42 (1979); accord Mills Music, Inc. v. Snyder, 469 U.S. 153, 164 (1985); Escondido Mutual Water Co. v. La Jolla Band of Mission Indians, 466 U.S. 765, 772 (1984).

were to pay the respondent the entire sum owed on the mortgage, his obligation would be satisfied. As in Davenport, it is petitioner's failure to make a monetary payment which gives rise to the creditor's remedy. Here, respondent may enforce the payment obligation by enforcing its security interest and proceeding against the petitioner's real estate. In Davenport, the remedy was the threat of revocation of probation and possible incarceration. The only difference between this case and Davenport is the manner in which the payment obligation is enforced and that difference is immaterial for purposes of determining whether an obligation is a claim under 11 U.S.C. §101(4). Davenport, 110 S.Ct. at 2131.

This analysis is buttressed by the qualifying language of §101(4) which makes

clear that a right to payment is a claim -- regardless whether it is "secured" or "unsecured." In this case, as the term is a commonly understood, respondent holds a "secured" claim. It has a right to receive money which is secured by a security interest in the petitioner's real property. Particularly since the modifying language of §101(4) is intended to be expansive rather than limiting, there can be little doubt that the petitioner's in rem obligation in this case easily falls within the literal terms of the statute. It goes against common sense, and would certainly be a shock to secured creditors whose claims against a debtor are discharged in a chapter 7 case, to say that such creditors have no "right to payment." The intent of the "right to payment" phrase is to limit bankruptcy courts to claims which

are reducible to fixed monetary amounts. Despite the discharge of personal liability, a secured creditor still has a right to the exact amount of the debt which may be obtained from the proceeds of a foreclosure sale.

In its opinion below, the court of appeals concluded that the respondent had no right to payment against the petitioner "because Johnson's personal liability on the mortgage was discharged under Chapter 7." Petition for Cert. App. 7. The lower court's fundamental error was to focus on the nature of the remedy available to respondent in determining whether a claim exists rather than simply evaluating whether the creditor has an enforceable remedy for the petitioner's failure to make payment.

The flaw in the court of appeals'

analysis is even more apparent when one considers that the primary distinction between personal and <u>in rem</u> liability has to do with the scope of the creditor's remedy for enforcing a right to payment. When a debtor has personal liability, any property owned by the debtor is potentially subject to sale if a debtor fails to make payment and a creditor obtains a money judgment and proceeds to execute on the judgment. By comparison, where a payment obligation is <u>in rem</u> and there is no personal liability, a creditor may proceed to enforce its security interest by seeking to foreclose and sell only specified property in which the debtor has transferred a property interest to the creditor. In both situations, our legal system contemplates that a creditor may subject a debtor's property to the process

of judicial or non-judicial execution in order to satisfy an unpaid obligation. As between the debtor and the creditor, the difference between personal and in rem liability does no more than define which property owned by the debtor is subject to sale to satisfy the indebtedness. Thus, the fact that a creditor can look only to specified property, rather than all of the debtor's property, cannot possibly make the debtor's obligation to pay any less a "right to payment". In essence, the difference between personal and in rem liability has to do with the scope of the creditor's remedy; it has no bearing in as to whether the creditor has a right, in the first place, to receive payment.

2. 11-U.S.C. §102(2)

This case can be resolved solely by reference to the plain language of §101(4).

That Congress meant what it said in that section is confirmed by reference to 11 U.S.C. §102(2). Section 102(2) provides the following rule of construction for the Bankruptcy Code:

> "claim against the debtor" includes claim against property of the debtor;

Through this plain, unambiguous language, Congress has made explicit that a claim against the debtor also encompasses a claim against the debtor's property. In light of the statute's reference to a claim against property of the debtor as being "included" within the concept of a claim against the debtor, §102(2) can only be read to mean that a claim against property is a type a claim cognizable in the debtor's bankruptcy case.

Moreover, §102(2) specifically uses the phrase "claim against the property of

the debtor." If Congress had intended an in rem obligation against the debtor's property to be something other than a claim, it would not have employed the defined term "claim" in enacting §102(2); Congress would have referred to a claim against the debtor as including a creditor's "rights" against a debtor's property, or some similar term.

Thus, §102(2) represents a clear expression of Congress' intent to include in rem obligations within the definition of a bankruptcy claim and eliminates any possible doubt on the question. Since there is no other language elsewhere in the Code to suggest that Congress intended to limit the applicability of §102(2) to certain types of in rem claims, the Court must give full expression to the plain meaning of the provision in construing

§101(4) in all cases. See 11 U.S.C. §103(a).

C. Congress' Intent to Include In Rem Obligations Within The Meaning Of The Term "Claim" Also Finds Clear Expression In 11 U.S.C. §502

Section 502 of the Bankruptcy Code provides that if a party files an objection to a proof of claim,

> the court . . . shall determine the amount of such claim . . . and shall allow such claim in such amount except to the extent that --
>
> (1) such claim is unenforceable against the debtor and property of the debtor, under any agreement or applicable law for a reason other than because such claim is contingent or unmatured . . . .

11 U.S.C. §502.

On its face, §502 demonstrates that Congress contemplated that an obligation enforceable only against the debtor's property is a bankruptcy "claim." Section 502 states that a claim shall be allowed by

the court unless it is unenforceable, under applicable law, against the debtor and his property. To be disallowed, a claim must be unenforceable against both the debtor and his property. Rephrasing this principle to positive voice, this means that if the claim is enforceable against either the debtor or his property, the claim must be allowed. Just as a creditor holding a claim only against the debtor personally has an allowable claim, so must a creditor holding a claim only against the debtor's property. Obviously, it would make no sense for Congress to provide that a claim must be allowed if enforceable against the debtor's property if an in rem obligation were not considered a claim.

Nothing in §502 or elsewhere in the Code suggests that Congress intended to limit in any way the principle that a claim

may be enforceable against property. Again, under basic principles of statutory construction, the Court should give full effect to Congess' language.

D. If The Court Looks Beyond The Plain Language Of The Statute, The Legislative History Demonstrates That Congress Intended To Take The Language Of Sections 101(4) and 102(2) From The Most Expansive Definition Of "Claim" In The Former Bankruptcy Act, A Definition Specifically Adopted To Include Claims Against Property Only

In its opinion below, the court of appeals acknowledged that the plain language of §102(2) provides that a claim against the debtor includes a claim against property of the debtor. However, the court referred to the Senate Report in the Bankruptcy Code's legislative history which states that §102(2) is intended to "cover nonrecourse loan agreements where the creditor's only rights are against the property of the debtor, and not against the

debtor personally." S. Rep. No. 95-989, 95th Cong., 2d Sess. 28 (1978). Seizing upon this language in the Senate Report, the court held, in effect, that the only in rem obligations which are bankruptcy claims are those which arise from a nonrecourse agreement and that petitioner's payment obligation to respondent, which may be enforced only against petitioner's property and not through personal liability due to the prior chapter 7 discharge, is not a bankruptcy claim. Petition for Cert. App. 5-6.

The lower court's reasoning is inconsistent with the canons of statutory construction this Court has applied in construing the Bankruptcy Code. The court of appeals limited the plain language of sections 101(4), 102(1) and 502(b) by relying on legislative history which did no

more than give an illustrative example of a claim against property of the debtor. Nothing in the committee reports or voluminous hearings suggest that there was any intent to limit the claims against property solely to those arising by agreement. In essence, the court construed a clear statute by reference to ambiguous legislative history. To the contrary, as this Court stated in Ron Pair, the plain meaning of the statute

> should be conclusive except in the "rare cases [in which] the literal application of a statute will produce a result demonstrably at odds with the intention of its drafters."

109 S.Ct. at 1031, quoting, Griffin v. Oceanic Contractors, Inc., 458 U.S. 564, 571 (1982).[4]

[4] Where Congress has employed statutory language which is open to interpretation and which, if construed to give effect to its apparent plain (continued...)

Thus, it was incorrect for the court of appeals to rely on a single passage from the legislative history as a basis for overriding the plain language of the statute. Further, as explained below, a

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[4](...continued)
meaning, would depart from clear pre-Code bankruptcy practice and would conflict with either other Code provisions or other significant state or federal interests, this Court has held that Congress did not intend to depart from pre-Code practices. See Midlantic National Bank v. New Jersey Department of Environmental Protection, 474 U.S. 494 (1986); Kelly v. Robinson, 479 U.S. 36 (1986). Here, by comparison, the applicability of the plain language of §101(4) and §102(1) to an in rem obligation is not open to interpretation and is consistent with §502(b). Moreover, the plain meaning of §101(4) and §102(2) are consistent with pre-Code practice. Most significantly, the courts had interpreted the former reorganization definition of claim under the prior Bankruptcy Act to include claims where there was no personal liability. Indeed, the leading cases did not involve non-recourse agreements. In both Herbert V. Apartments Corp. v. Mortgage Guarantee Corp., 98 F.2d 662, 666 (3d Cir. 1938), cert. denied, 305 U.S. 640 (1938) and Brooklyn Trust Co. v. R.A. Securities Holding, Inc., 134 F.2d 165 (2d Cir. 1943), the debtors had no agreement with creditors who had mortgages on their property. Rather, in both cases the debtor had purchased the property subject to the mortgage but without agreeing to assume the debt.

more comprehensive review of the legislative history reveals that Congress fully understood that the broadest possible definition of claim enacted into the Bankruptcy Code would include claims against the property of the debtor. It is therefore not surprising that at least three authoritative commentators on the Bankruptcy Code have all agreed that the Code definition of the term "claim" encompasses the in rem mortgage obligation which survives the discharge of a debtor's personal liability in a chapter 7 case. 5 Collier on Bankruptcy ¶1322.09, at 1322-19 (15th ed. 1990); W. Drake and J. Morris, Chapter 13 Practice and Procedure 59.08, at 5-81 (supp. 1990); Norton Bankruptcy Law and Practice 574.08, at 74-46 (1990).

1. The definition of "claim" in Chapter X of the Previous Bankruptcy Act was adopted to assure that claims against property only could be included in bankruptcy proceedings

In 1938, the Chandler Act, Pub. L. No. 696, 75th Cong., 52 Stat. 883, added to the Bankruptcy Act of 1898, the predecessor to the present bankruptcy statute, definitions of "claim" for various chapters of that Act. The most expansive was that of section 106(1) for Chapter X on Corporate Reorganizations.[5]

> " 'claims' [when used for the purposes of Chapter X] shall include all claims of whatever character against a debtor **<u>or its property</u>**, except stock, whether or not such claims are provable under section 63 of this Act and whether secured or unsecured, liquidated or unliquidated, fixed or contingent".

[5] The same definition was used in Chapter XII -- Real Property Arrangements by Persons Other Than Corporations. § 406(2), codified at 11 U.S.C. § 806(2) (1976). Essentially the same definition was used in Chapter IX -- Adjustment of Debts of Political Subdivisions... § 81(1), codified at 11 U.S.C. § § 401(1). Other definitions added by the Chandler Act were more restrictive. For Chapter XI-- Arrangements, the definition included only claims against the debtor. § 307(2), codified at 11 U.S.C. § 707(2) (1976). For Chapter XIII-- Wage Earner Plans, "claims" excluded claims secured by real property or "chattels real." § 606(1), codified at 11 U.S.C. § 1006(1) (1976).

§ 106(1), Bankruptcy Act of 1898, as added June 22, 1938, ch. 575 § 1, 52 Stat. 883 codified at 11 U.S.C. § 506 (1976) (emphasis added).

The definition of "claim" was added for the specific purpose of reversing earlier decisions such as <u>In re Draco Realty Corp.</u>, 11 F.Supp 405 (S.D.N.Y. 1935), which held that creditors with claims only against a debtor's property could not bring involuntary bankruptcies. <u>See</u> Gerden, <u>Corporate Reorganizations, Changes Effected by Chapter X of the Bankruptcy Act</u>, 52 Harv. L. Rev. 1, 4 (1939). The Committee Reports on the Chandler Act explained the purpose of the

new definition.

The House of Representatives' Report stated:

> The provisions dealing with the right to initiate a reorganization proceeding are uncertain...The phrase 'claims against any corporation' has been construed to exclude creditors holding claims against the property of the debtor. This is unnecessarily restrictive and should be corrected.

H.R. Rep. No. 75-1409, 75th Cong. 39 (1937), cited in Matter of Sponsor Realty Corp., 48 F.Supp 735, 738 (S.D. N.Y. 1943).

The Senate Report stated:

> The right of creditors to file petitions is restricted to creditors holding claims that are liquidated in amount and fixed in liability...These need not be claims against the debtor itself but may be claims against the property of the debtor.

S. Rep. No. 75-1916, 75th Cong. 25 (1938) (emphasis added), cited in, Sponsor Realty, 48 F.Supp at 738.

2. By 1977, it was settled law that claims in reorganizations included claims with no in personam rights

Following passage of the Chandler Act, courts consistently interpreted "claim" under Chapter X of the Bankruptcy Act to include claims against property only. In the leading case of Herbert V. Apartments Corp. v. Mortgage Guarantee Corp., 98 F.2d 662, 666 (3d Cir. 1938), cert denied, 305 U.S. 640 (1938), the debtor owned property which its successors had mortgaged without personal liability. The court held that the mortgage holders had a "claim" against the debtor which could be dealt with in the bankruptcy. Accord Brooklyn Trust Co. v. R.A. Securities Holding, Inc., 134 F.2d 165 (2d Cir. 1943); Sponsor Realty Corp.

By the time the present Act was being considered, the broad scope of the Chapter X definition was settled law. Collier on

Bankruptcy, the leading commentary on the Act stated:

> The word "claims" as defined in § 106(1) [of Chapter X of the Bankruptcy Act] is sweeping in scope. Within its purview is any character of a claim against the debtor or its property, whether or not such claim is provable under § 63 of the Act, and whether secured or unsecured, liquidated or unliquidated, fixed or contingent. This is, of course, a more inclusive definition than that applicable in ordinary bankruptcy and it should be given a broad construction with respect to claims and creditors in order to dispose of all liabilities of the debtor in reorganization.
>
> To come within the terms of § 106(1), however, it is essential that the claim in question be predicated against either the debtor or the debtor's property. But it is to be noted that a claim against the debtor's property alone is sufficient. It is not necessary that the claimant have an in personam claim against the debtor, and such a provision in the Act is clearly constitutional.

6 Collier on Bankruptcy ¶2.05 pp. 306-307

(14th ed. 1978) (citations omitted) (emphasis added).

3. The present definition of claim in sections 101(4) and 102(2) is taken from and expands on the already broad Chapter X definition

The present definition of "claim" in section 101(4) and the accompanying rule of construction in section 102(2) were adopted as part of the Bankruptcy Reform Act of 1978, Pub. L. 95-598, §§ 101(4) & 102(2), 92 Stat. 2549, 2550, 2555. The early versions of the bills which ultimately became the final 1978 Act employed a more narrow definition. See Appendix Vol. 2 Collier on Bankruptcy, "Legislative History of the New Bankruptcy Law," (15th ed. 1990) (tracing the various bills and proposals which preceded the 1978 Act).*

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* H.R. 31, the "Commission's Bill" and H.R. 32, " the "Judges' Bill" both defined "claim" as a "legally enforceable demand for performance of (continued...)

H.R. 8200 reported to the House on September 9, 1977, introduced a more sweeping definition along with the present numbering. This definition was:

> §101(4) "Claim" means -
> (A) right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured; or
> (B) right to an equitable remedy for breach of performance if such breach does not give rise to a right to payment, whether or not such right to an equitable remedy is reduced to judgment fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured;

H.R. 8200, 95th Cong. 1st Sess. reported

(...continued)
an obligation to pay money". H.R. 31 § 1-102(9), 94th Cong. 1st Sess. (1975) and H.R. 32 § 1-102(7), 94th Cong, 1st Sess. (1975), both reprinted in Hearings Before the Subcomm. on Civil and Constitutional Rights of the Comm. on the Judiciary on H.R. 31 and 32, 94th Cong. 1st & 2d Sess. Appendix p. 15 (1976).

September 8, 1977, reprinted in Appendix Vol. 3 Collier on Bankruptcy III-1,309-10 (15th ed. 1990).

This broader definition was adopted along with a "Rule of Construction" in section 102(2) which stated that "claim against the debtor" includes claim against property of the debtor." Id. at III- 322.

Although H.R. 8200 divided the definition into a main definition and a rule of construction, both track almost word for word the Chapter X definition of the old Section 106, but broaden it to include equitable claims and rights for breach of performance. While subsequent drafts narrows slightly the definition in section 101(4)(B), the language of the

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The final version §101(4)(B) simply incorporated a requirement that an equitable remedy must give rise to a right to payment to be a "claim."

rule of construction that a claim includes claim against the property of the debtor remained unchanged and was enacted into law.

The House Committee Report on H.R. 8200 and the Senate report on S.2266 explicitly acknowledged the reorganization sections of the prior Bankruptcy Act as the source of the new definition of claim and also emphasized that the new definition was even broader than under prior law:

> Under present law, 'claim' is not defined in straight bankruptcy. ... the term is defined in the debtor rehabilitation chapters of present law far more broadly. The definition in paragraph (4) adopts an even broader definition of claim than is found in the present debtor rehabilitation chapters.

H.R. Rep. No 95-595, 95th Cong. 1st Sess. 309 (1977) (emphasis added) ("House Report"); S. Rep No. 95-989, 95th Cong. 2d

Sess. 21-22 (1978) (emphasis added).

Thus, the present definition of "claim" was taken from the existing Chandler Act definition for reorganizations. That definition had been explicitly adopted in order to encompass claims where there was no in personam right. By 1977, the broad scope of that definition was supported by more than thirty years of settled judicial interpretation that claims included claims exclusively against property. Congress intended, by broadening the scope of the definition even further, to include within its scope at least all claims included by the Chandler Act definition, including those exclusively against property of the debtor.

Finally, where Congress did intend to limit the scope of section 102(2), it did

so explicitly. The present provisions on involuntary bankruptcy in section 303(b) adopted in 1978 along with sections 101 and 102, limit the right to bring involuntary cases to holders "of a claim against such person" (emphasis added). Thus, as Collier points out, Congress here did target a narrow exception to section 102(2) so that a creditor holding a mortgage, but not a personal claim, could not bring an involuntary petition, but would then have a "claim" once the order of relief was entered. 2 Collier on Bankruptcy ¶303.08 p.393-25 (15th ed. 1990). Had Congress intended other limitations on the scope of §102(2), there would be some evidence of that intent and Congress would have explicitly incorporated the limitation in the statute.

II. THE *PER SE* RULE ADOPTED BY THE COURT OF APPEALS EXCLUDING ALL NONRECOURSE MORTGAGES FROM CHAPTER 13 RELIEF IS INCONSISTENT WITH THE PURPOSES AND POLICIES OF THE CODE AND IS NOT NECESSARY TO CORRECT ABUSES OF THE BANKRUPTCY SYSTEM

A. Introduction

In the courts below, respondent Bank has suggested that Johnson's utilization of a chapter 13 bankruptcy to save his farm is somehow an abuse of the bankruptcy system. It is presumed that respondent will again raise this issue before this Court.

For the reasons discussed in the sections above and in petitioner's brief, Johnson's use of chapter 13 is perfectly proper. Although the Code sets forth certain provisions regarding eligibility or disqualification for bankruptcy relief, nowhere does it prohibit the use of chapter 13 to pay a residential mortgage obligation where personal liability has been

discharged. However, even if there is a legitimate question as to the propriety of Johnson's filing, the Bankruptcy Code provides the bankruptcy court with ample tools to prevent abuse of the bankruptcy system.

B. **The Purpose And Policies Of Chapter 13**

The two principal purposes of bankruptcy are to provide equity among creditors and a fresh start for the debtor. The fresh start purpose is designed to allow individuals who have become mired in debt to free themselves from that burden and engage in newly productive lives unhampered by the pressure and discouragement of preexisting debt. E.g., Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934). The goal of equity among creditors is achieved by the fair distribution of the debtor's assets according to established

rules, set forth in the Code, which guarantee similar treatment to similarly situated creditors. See e.g., House Report at 117-78.

In substantially revising chapter 13 of the Bankruptcy Code in 1978, Congress clearly expressed its intent to make consumer debtor rehabilitation payment plans an attractive and flexible alternative to the straight liquidation of chapter 7 and to address the problems which had caused former Chapter XIII to be under-utilized under the Act. See House Report at 116-118. As in the other Code chapters, under chapter 13, Congress sought to accommodate fairly both debtors and creditors and to achieve a balance of the competing interests which arise in bankruptcy cases. House Report at 118. See also 5 Collier on Bankruptcy ¶1300.02

(15th ed. 1990). The applicable Code provisions accord significant rights to both debtors and creditors. The creation of such a delicately balanced system obviates the need for the ironclad *per se* rule urged by respondent - a holding that would exclude entirely an important class of monetary obligations (residential mortgages where there is no personal liability) from the comprehensive system of administering debts found in chapter 13.

When this system is examined closely, it is apparent that the Code either accommodates or rejects the concerns of the respondent that petitioner's chapter 13 filing is an abuse of the bankruptcy system. What chapter 13 provides is the opportunity for an individual to propose a financial rehabilitation plan which will provide for payment of a secured creditor's

claim and, in many cases, save the debtor's home.

C. The Code Provides Ample Tools To Prevent Alleged Abuse

1. The Code contains *per se* rules where Congress found them necessary

Where Congress has found it necessary to include express proscriptions on debtors, it has done so. The Code contains several *per se* rules regarding eligibility for bankruptcy relief.

a. 11 U.S.C. §109(e)

Section 109(e) of the Code sets forth the standards of eligibility for chapter 13 relief. The section states:

> (e) Only an individual with regular income that owes, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts of less than $100,000 and noncontingent, liquidated, secured debts of less than $350,000, or an individual with regular income and such individual's spouse, except a stockbroker or a commodity

broker, that owe, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts that aggregate less than $100,000 and noncontingent, liquidated, secured debts of less than $350,000 may be a debtor under chapter 13 of this title

The eligibility criteria in §109(e) are specific and restrictive. The limitations on amount of debt were intended to insure that chapter 13 can only be used by those for whom it was designed. The underlying purpose of the section was to establish the dollar limitations on indebtedness that an individual with regular income can incur and yet file under chapter 13. S. Rep. No. 989, 95th Cong., 2d Sess 31 (1978). See 2 Collier on Bankruptcy ¶109.05 (15th ed. 1990).

Section 109(e) sets forth clearly delineated standards of eligibility for chapter 13. There is no provision for the

judicial exercise of discretion. If the court finds that a debtor fails to meet those standards, chapter 13 relief may be denied upon motion of any party in interest. In re Fostvedt, 823 F.2d 305 (9th Cir. 1987).

b. 11 U.S.C. §109(g)

Congress added another per se rule of ineligibility for bankruptcy relief to §109 in 1984 when it acted to rectify the perceived abuse of multiple bankruptcy filings. The additional provision, §109(g), states as follows:

> (g) Notwithstanding any other provision of this section, no individual or family farmer may be a debtor under this title who has been a debtor in a case pending under this title at any time in the preceding 180 days if -
>
> (1) the case was dismissed by the court for willful failure of the debtor to abide by orders of the court, or to appear before the court in proper prosecution of

the case; or

> (2) the debtor requested and obtained the voluntary dismissal of the case following the filing of a request for relief from the automatic stay provided by section 362 of this title.

Prior to the enactment of §109(g), some debtors had been using tactics that could be deemed abusive. Such an issue would arise, for example, where a debtor, after the dismissal of an earlier case, filed a second bankruptcy on the eve of foreclosure solely to re-invoke the benefits of the automatic stay, 11 U.S.C. §362(a), and without any legitimate reorganization purpose. See 5 Collier on Bankruptcy ¶1300.12 at 1300-49. Prior to 1984, the propriety of the second filing would have been evaluated in the context of the requirement of good faith. 11 U.S.C. §1325(a)(3). In re Johnson, 708 F.2d 865, 868 (2d Cir. 1983).

Now, with §109(g), Congress has specified the point at which repetitive filings automatically become an abuse of the bankruptcy system." Section 109(g) only applies when the particular circumstances described therein are present.

In the case before this Court, Johnson's earlier chapter 7 case had been terminated almost two years before he filed the chapter 13 case. Furthermore, the chapter 7 case had proceeded to discharge and had been closed; it had not been dismissed under any of the circumstances delineated in §109(g). Applying the benchmark established by Congress in

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In re March, 83 B.R. 270, 274 (Bankr. E.D.Pa. 1988) ("The existence of section 109(g) provides congressional guidance on the circumstances under which repetitive filings are inappropriate and thus limits the need for the court to examine repetitive filings under the rubric of good faith.").

§109(g), then the second filing was not _per se_ improper. To the extent, if any, that the second filing raised a question of good faith, that was an issue for the bankruptcy court to resolve.

c. 11 U.S.C. §727(a)(8), (9)

Section 727 of the Code is yet another area where Congress has implemented a bright line rule on eligibility for bankruptcy relief. This section sets forth a number of requirements for the granting of a chapter 7 discharge, and provides in

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This is not to say that repetitive filings, even if not fitting within the parameters of §109(g), may not constitute evidence of lack of good faith to the extent that they reflect the debtor's intent to misuse the relief available under the Code. _See_ _In re Penz_, 121 B.R. 602 (Bankr. E.D.Okl. 1990) (four serial filings were in bad faith and warranted dismissed with prejudice to refiling for 180 days); _In re Kinney_, 51 B.R. 840 (Bankr. C.D.Ca. 1985) (ten filings by different members of one family solely to utilize automatic stay without intent or ability to effectively reorganize constituted bad faith; monetary sanctions imposed on attorney).

pertinent part as follows:

> (a) the court shall grant the debtor a discharge, unless -
>
> . . .
>
> (8) the debtor has been granted a discharge under this section, under section 1141 of this title, or under section 14, 371, or 476 of the Bankruptcy Act, in a case commenced within six years before the date of the filing of the petition;
>
> (9) the debtor has been granted a discharge under section 1228 or 1328 of this title, or under section 660 or 661 of the Bankruptcy Act, in a case commenced within six years before the date of the filing of the petition, unless payments under the plan in such case totaled at least -
>
> (A) 100 percent of the allowed secured claims in such case; or
>
> (B)(i) 70 percent of such claims; and
>
> (ii) the plan was proposed by the debtor in good faith, and was the debtor's best effort; ...

Thus, §727(a)(8) and (9) establish a _per se_ rule governing how often a debtor

can obtain the benefits of the chapter 7 discharge. Such a discharge cannot be granted if a previous chapter 7 discharge was obtained in a case commenced within the previous six years or if a chapter 13 discharge was obtained in the same time frame where the chapter 13 plan paid less than 70% of the allowed secured claims. See generally, In re Marshall, 74 B.R. 185 (Bankr. N.D.N.Y. 1987); Matter of Bishop, 74 B.R. 677 (Bankr. M.D.Ga. 1987).

2. **The Code enables courts to exercise discretion where necessary to prevent abuse**

In addition to the statutory per se rules that limit debtor conduct as discussed above, the Code also contains more general provisions that require the exercise of judicial discretion to prevent abuse of the bankruptcy system.

a. 11 U.S.C. §1325(a)(3)

Perhaps the most important protection against abuse of the Bankruptcy Code in chapter 13 cases is the bankruptcy court's power to deny confirmation of a plan which has not been proposed "in good faith." 11 U.S.C. §1325(a)(3).

In one of the earliest cases construing §1325(a)(3), Judge William L. Norton, Jr., a respected authority on the Code,[10] analyzed this provision and concluded as follows:

> Two elements seem inherent in "good faith" with respect to the debtor's responsibility in proposing a plan, to wit: (a) honesty in purpose and (2) full disclosure of relevant facts.
>
> . . .
>
> Thus, good faith as used in section 1325(a)(3) means full and complete disclosure and honesty

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[10] See Norton Bankruptcy Law and Practice (1990).

> of purpose by the debtor to consummate the payments proposed in the plan.

In re Wiggles, 7 B.R. 373, 380 (Bankr. N.D.Ga. 1980). See also Barnes v. Whelan, 689 F.2d 193, 198 (D.C. Cir. 1982) (good faith refers to "debtor misconduct in the implementation or approval of the plan, and did not relate to the contents of the plan.") (emphasis in original).

The courts of appeals have outlined a list of factors which bankruptcy courts should consider in determining whether a chapter 13 plan has been proposed in good faith. The widely accepted view is that only where there has been a showing of serious debtor misconduct or abuse should a chapter 13 plan be found lacking in good

E.g., In re LeMaire, 883 F.2d 1373 (8th Cir. 1989); In re Smith, 848 F.2d 813 (7th Cir. 1988).

faith. Courts have not hesitated to deny confirmations of plan which did not satisfy the good faith requirement.

In the bankruptcy court below, respondent Bank availed itself of its right to file an objection to confirmation of Johnson's chapter 13 plan. See Bankr. Rule 3020(b). The bankruptcy court carefully reviewed the objection and found no basis for concluding that the plan was not proposed in good faith. In re Johnson, No. 87-10585 (Bankr. D.Kan. 1988) (slip op. at 13). Neither the district court nor the court of appeals reached the issue. However, should this matter be remanded for a determination of good faith, the

Education Assistance Corp. v. Zellner, 827 F.2d 1222, 1227 (8th Cir. 1987). See 5 Collier on Bankruptcy ¶1325.04[3] (15th ed. 1990).

In re Waldron, 785 F.2d 936 (11th Cir. 1986); In re Chinichian, 784 F.2d 1440 (9th Cir. 1986).

bankruptcy court's finding would be subject to review under the clearly erroneous standard. In re Herd, 840 F.2d 757 (10th Cir. 1988).

Indeed, the two courts of appeals which have addressed the legality of following a chapter 7 bankruptcy with a chapter 13 case have done so within the context of the good faith requirement. In re Saylors, 869 F.2d 1434 (11th Cir. 1989); In re Metz, 820 F.2d 1495 (9th Cir. 1987). In both cases, the courts sustained the evidentiary findings that the chapter 13 plans were proposed in good faith. Saylors, 869 F.2d at 1438; Metz, 820 F.2d at 1498-1499.

b. 11 U.S.C. §105(a)

The Code states that bankruptcy courts may "issue any order, process or judgment that is necessary or appropriate to carry

out the provisions" of Title 11. 11 U.S.C. §105(a). The bankruptcy court is specifically empowered to prevent abuse of process sua sponte. Id. As this Court has recently recognized, this provision of the Code is consistent with

> "the traditional understanding that bankruptcy courts, as courts of equity, have broad authority to modify creditor-debtor relationships."

U.S. v. Energy Resources Co., Inc., 110 S.Ct. 2139, 2142 (1990) (citations omitted).

Section 105(a), with its grant of general equitable powers, may be used to remedy any abuse of the bankruptcy process which a debtor might attempt to commit, as long as those powers are exercised within the confines of the Code. Norwest Bank Worthington v. Ahlers, 485 U.S. 197 (1988); Official Comm. of Equity Sec. Holders v.

Mabey, 832 F.2d 299, 302 (4th Cir. 1987). Thus, §105(a) provides an additional ground for the exercise of judicial discretion to sanction a debtor's abuse of the bankruptcy process and effectuate the purposes of the more specific proscriptions on debtor misconduct contained in the Code, where such action may be necessary.

In short, where Congress has found it necessary to legislate specific per se limitations on debtor eligibility for relief under the Code, it has done so. If Congress had wanted to prohibit a debtor from filing a chapter 13 bankruptcy to pay a mortgage where there is no personal liability for the debt, Congress would certainly have included that prohibition in the Code. The fact that Congress did not do so must mean that Johnson's attempt to use chapter 13 to save his farm is not per

se inappropriate.

However, should Johnson's chapter 13 filing raise a legitimate issue of good faith, as respondent argues that it does, then that is a question for the bankruptcy court to decide in the first instance. If necessary, this case can be remanded on that issue. But perceived abuse cannot be remedied by a strained reading of the Code which pronounces that Johnson and innumerable other debtors can never use chapter 13 to pay claims against their properties.

III. THE RULE ADOPTED BY THE COURT BELOW WOULD SEVERELY IMPAIR THE AVAILABILITY OF BANKRUPTCY RELIEF FOR CONSUMER DEBTORS IN BOTH CHAPTER 13 AND CHAPTER 7 CASES

One of the most common and important reasons for the filing of chapter 13 bankruptcy cases by consumer debtors is the desire to save a family's home, usually

through curing a mortgage delinquency pursuant to section 1322(b)(5) of the Bankruptcy Code. A decision by this Court affirming the decision of the Court of Appeals in this case would render chapter 13 unavailable to a large number of families who need its relief in order to save their homes, and would also deter the filing of chapter 7 cases by homeowners needing a bankruptcy fresh start.

The frequent use of chapter 13 to save families' homes has been noted both by courts and commentators. For example, in Matter of Brunson, 87 B.R. 304, 307 (Bankr. D.N.J. 1988) the court noted that 70% to 80% of the chapter 13 cases filed in New Jersey represented debtors' attempts to save their homes. The intent of Congress to make chapter 13 available for the curing of home mortgages is described in Collier on

Bankruptcy 1322.09[2] as well as the fact that "its most common use by far is to cure defaults on residential mortgages."1322.09[1]. Norton Bankruptcy Law and Practice §§74.08 describes section 1322(b)(5) as "much used by chapter 13 debtors to cure defaults and reinstate home mortgages that are in default on the date of the petition." A recent comprehensive study of bankruptcy debtors concluded its discussion of homeowners in bankruptcy by stating "[t]he picture of homeowners in bankruptcy is one of people struggling to keep their homes." Sullivan, Warren and Westbrook, As We Forgive Our Debtors 143 (1989) (hereinafter "Sullivan").

The holding of the court below would deny the use of chapter 13 for this purpose to all debtors who were not personally liable on the mortgages on their homes,

going far beyond simply the class of debtors who had previously filed chapter 7 bankruptcy cases. In the experience of the writers of this brief, many other homeowners have no personal liability to the holders of mortgages on their homes.

For example, a child who inherits a family home from a parent who passes away rarely formally assumes the mortgage which encumbers that property. Typically, the home remains in the family as the residence of the child and often grandchildren. However, the original mortgage and note, signed only by the deceased parent, may fall into default, either during the financial disarray which ensues upon the parent's death or at some time thereafter.

Similarly, a divorcing spouse who, through equitable distribution, obtains title to a home that was formerly in the

name of the other spouse typically never becomes obligated on an existing mortgage. A major factor in bringing about such title transfers is the presumption, under many equitable distribution statutes, in favor of awarding the family home, or at least a possessory interest therein, to the spouse (usually the wife) who will have custody of the couple's children. Again, the financial dislocation connected with a divorce and the couple's sudden need to support two households rather than one may leave a mortgage in default, or the spouse who acquires title or some lesser interest may have financial difficulties causing a default at some later time.

In many community property states, community property belonging to both spouses is liable for debts incurred by either spouse. This liability can follow

the property even after a divorce, creating another situation where a debtor's home may liable for a debt even though the debtor has no personal liability. See Britt v. Damson, 334 F.2d 896 (9th Cir. 1964); In re Chenich, 87 B.R. 101 (Bankr.9th Cir. 1988). Still other examples are the grandmother who gives a mortgage on her home to secure a grandchild's purchase of a used car or the spouse who signs a mortgage to secure a loan to the other spouse's business.

In all of these situations, chapter 13 relief would be denied by the ruling below because the debtors had no personal liability to the holder of the mortgage. The purpose of Congress to provide effective bankruptcy relief to these families would be thwarted, despite the total absence of any provision in the Code dictating that result.

Moreover, the holding of the court below would also greatly deter the filing of chapter 7 bankruptcy cases by homeowners. Studies have consistently showed that a large number of homeowners file chapter 7 bankruptcy cases. Sullivan supra, at 139; Shuchman, The Average Bankrupt: A Description and Analysis of 753 Personal Bankruptcy Filings in Nine States, 88 Commercial L.J. 238, 302 (1983). Whether because their mortgage is the one debt they faithfully paid when they could pay no others or because the discharge of other debts in chapter 7 allows them to catch up on delinquent mortgage payments without the additional complexity and expense of chapter 13, many homeowners are able to obtain their bankruptcy fresh start through chapter 7.

These debtors would certainly have to

think twice about utilizing chapter 7 relief if they knew that they were forever giving up their right to later save their homes from foreclosure in chapter 13, not just soon after their chapter 7 cases, or within six years after the chapter 7 cases, but at anytime during the twenty to thirty year terms of their mortgage loans. Worse yet, many debtors would probably file chapter 7 cases unaware that they were waiving this important right, perhaps only to find out years later when they were in desperate need of it. In either case, the availability of chapter 7 to provide a true fresh start to hard-pressed families and individuals is greatly impaired.

Nor is it of any solace that a debtor may sometimes reaffirm a debt after bankruptcy thereby maintaining a personal liability. A reaffirmation is effectuated

only by an agreement between the debtor and the creditor. A debtor may not unilaterally create a reaffirmation agreement. Matter of Vinson, 5 B.R. 32 (Bankr.N.D.Ga. 1980). If mortgage lenders become aware that chapter 7 debtors will be unable ever to file chapter 13 cases dealing with their loans if they do not reaffirm, there are likely to be few mortgage lenders who will have any incentive to agree to reaffirmations. It is the experience of the writers of this brief that in fact mortgage lenders virtually never pursue deficiency judgments, so that the personal liability obtained through a reaffirmation is essentially worthless to them.

In any case, it is hard to believe that Congress could have intended to place in the hands of mortgage lenders the right

to determine whether their borrowers who filed chapter 7 bankruptcy cases would ever be able to use chapter 13 with respect to their mortgages. As discussed elsewhere in this brief, nothing in the plain language or legislative history even suggests such a result, which is at odds with the basic purposes intended by Congress for chapter 13 bankruptcy cases.

It has often been said that hard cases make bad law. The Court should be aware that the debtor in this case has little in common with most consumer debtors who would use chapter 13. The typical consumer bankruptcy debtor does not have income from oil and gas leases or other income to make plan payments of $35,000 a year, and never had mortgage debts of close to $300,000. The median income of bankruptcy debtors is only about two-thirds of the national

median income and the median mortgage debt of bankruptcy debtors in 1981 was under $24,000. Sullivan supra at 64-69.

It may well be that, because of the proposed $80,000 balloon payment at the conclusion of the plan, or for other reasons, the debtor's plan in this case is not feasible. 11 U.S.C. §§1325(a)(6). See Collier on Bankruptcy 1325.07; Matter of Brunson, supra (plan calling for large balloon payment at conclusion of plan not feasible). It may also be that the plan was not proposed in good faith. These issues may be dealt with on remand from this court. However, the decision of the court below, which would close the courthouse door to large numbers of debtors needing chapter 13 relief, should be reversed.

IV. CONCLUSION

For the foregoing reasons, amici curiae request this Court to reverse the judgment of the court of appeals.

Respectfully submitted,

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